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15 IN THE UNITED STATES BANKRUPTCY COURT
16 FOR THE NORTHERN DISTRICT OF CALIFORNIA
17 SAN FRANCISCO DIVISION

18 **In re:**

19 **PG&E CORPORATION**

20 And

21 **PACIFIC GAS AND ELECTRIC
22 COMPANY,**

23 Debtor.

- 24 ☐ Affects PG&E Corporation
25 ☐ Affects Pacific Gas and
26 Electric Company
27 ☒ Affects both Debtors
28

CASE NO. 19-30089(DM)

Chapter 11

(Lead Case)
(Joint Administered)

**CALIFORNIA DEPARTMENT OF
WATER RESOURCES' MOTION FOR
ORDER DETERMINING THAT THE
CASTLE ROCK AGREEMENT WITH
PG&E CANNOT BE ASSUMED AND
THAT THE DEPARTMENT OF WATER
RESOURCES' CLAIM NO. 78104 BE
PAID**

Date: March 2, 2022
Time: 10:00 a.m.
Place: Courtroom 17
Judge: Dennis Montali

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1 The California Department of Water Resources, by and through the State Water Project
2 (“DWR”), hereby moves the Court for an order determining that: (1) DWR’s cotenant interest in
3 the Castle Rock Agreement (defined below) terminated on its own terms, effective August 1, 2019,
4 based on DWR’s July 30, 2018, written notice to Pacific Gas & Electric Company (“PG&E”) and
5 the other cotenants to the Agreement; (2) the terms of the Castle Rock Agreement did not require
6 that DWR pay for any future estimated costs of removing the transmission line before its
7 termination from the Agreement could become effective; (3) because DWR’s termination of its
8 cotenant interest in the Castle Rock Agreement became effective on August 1, 2019, it is not an
9 executory contract that could have been assumed by Co-Debtors PG&E and PG&E Corporation in
10 connection with the Plan and Confirmation Order (both terms defined below) on June 19, 2020; (4)
11 DWR’s proof of claim No. 78104 in the principal amount of \$101,026.75 for a refund of prepaid
12 annual operating and maintenance expenses under the Castle Rock Agreement should be paid with
13 post-petition interest under the Plan; (5) the arbitration provisions contained in the Castle Rock
14 Agreement do not preclude the Court from determining whether DWR’s proof of claim should be
15 paid;¹ and (6) for such other and further relief as the Court deems just.

16 This Motion is based on section 365 of the Bankruptcy Code, Rule 6006 of the Federal
17 Rules of Bankruptcy Procedure, Rule 6006-1 of the Bankruptcy Local Rules of the United States
18 Bankruptcy Court for the Northern District of California and the Court’s authority over unresolved
19 Contract Assumption or Rejection Disputes reserved in Article VIII of the Debtors’ and
20 Shareholder Proponents’ Joint Chapter 11 Plan of Reorganization dated June 19, 2020 (Dkt. 8048)
21 (the “Plan”) and this Court’s retained jurisdiction, as specified in paragraphs 32 through 35, 67 and
22 78 of the Order Confirming Debtors’ and Shareholder Proponents’ Joint Chapter 11 Plan of
23 Reorganization dated June 19, 2020 (Dkt. 8053) (“Confirmation Order”). This Motion also is
24 related to and supplements the California State Agencies’ Objection to Schedule of Executory
25 Contracts and Unexpired Leases to be Assumed Pursuant to the Plan and Proposed Cure Amounts
26 (Dkt. 7276) and constitutes a Contract Assumption or Rejection Dispute that remains unresolved,

27 ¹ DWR raises the arbitration issue because it anticipates that PG&E may raise it in its
28 opposition to this Motion. DWR reserves the right to supplement its arguments on the arbitration
issue in its reply.

1 as provided in paragraph 32(c) of the Confirmation Order.

2 The Motion is supported by the Declaration of Ghassan AlQaser (“AlQaser Declaration”)
3 and the exhibits thereto, all other pleadings and papers cited or submitted herewith, and the
4 pleadings, filings and documents in the Debtors’ cases. In support of the Motion, DWR respectfully
5 represents as follows:

6 I. JURISDICTION

7 The Court has jurisdiction over this Motion pursuant to section 11.1 of the Plan, paragraphs
8 32 through 35, 67 and 78 of the Confirmation Order, 28 U.S.C. sections 157 and 1334, the Order
9 Referring Bankruptcy Cases and Proceedings to Bankruptcy Judges, General Order 24 (N.D. Cal.)
10 and Rule 5011-1(a) of the Bankruptcy Local Rules. This is a core proceeding pursuant to 28 U.S.C.
11 section 157(b).

12 Paragraph 34(a) of the Confirmation Order specifically reserves jurisdiction in this Court to
13 resolve any “Cure Disputes” as follows (emphasis added):

14 34. Determination of Cure Disputes.

15 a. Pursuant to Section 8.2(c) of the Plan, **in the event of an unresolved dispute**
16 **regarding** (i) any Cure Amount, (ii) the ability of the Reorganized Debtors or any
17 assignee to provide “adequate assurance of future performance” (within the meaning
18 of section 365 of the Bankruptcy Code) under the executory contract or unexpired
19 lease to be assumed, or (iii) **any other matter pertaining to assumption,**
assumption and assignment, or the Cure Amounts required by section 365(b)(1)
of the Bankruptcy Code (each, a “Cure Dispute”), such Cure Dispute shall be
resolved by a Final Order of the Court, which may be entered after the Effective
Date.

20 See also, Plan at ¶ 8.2(c). Further, paragraph 67(d) of the Confirmation Order also specifically
21 reserves jurisdiction in this Court to resolve any disputes over the assumption of executory contracts
22 involving Governmental Parties, including DWR as follows (emphasis added):

23 67. Governmental Performance Obligations.

24 d. Notwithstanding anything in this Confirmation Order, the Plan, or the Plan
25 Documents, the listing of a matter as an “executory contract” or an “unexpired lease”
26 in the Debtors’ schedules or Plan Documents (a “Potentially Assumed
27 Contract/Lease”) is without prejudice to any contention by any Governmental Unit
28 that the matter is not in fact an executory contract or unexpired lease as set forth in
section 365 of the Bankruptcy Code. With respect to any Cure Amount for a
Potentially Assumed Contract/Lease for which the United States or any department,
agency, or instrumentality of the State of California (collectively, the “Governmental
Parties”) is listed as the Non-Debtor Counterparty, all parties reserve all rights to

1 dispute such Cure Amount. **If any Governmental Party disputes (i) that any**
2 **Potentially Assumed Contract/Lease is in fact an executory contract or**
3 **unexpired lease or (ii) any Cure Amount, such Governmental Party shall have no**
4 **later than ninety (90) days after the Confirmation Date (or such later date as may be**
5 **mutually agreed upon between the applicable Governmental Party and the Debtors**
6 **or Reorganized Debtors) to file and serve an objection setting forth such dispute, and**
7 **any such dispute shall be resolved by the Bankruptcy Court.**

8 Further, paragraph 78 of the Confirmation Order provides that this Court retains jurisdiction
9 with respect to all matters arising from or related to the implementation of the Confirmation Order.
10 (“The Court shall retain jurisdiction with respect to all matters arising from or related to the
11 implementation of this Confirmation Order and as provided in Section 11.1 of the Plan.”).

12 **II. ISSUES PRESENTED/REQUESTED RELIEF**

13 Did DWR give proper notice that it was terminating its participation in the Agreement of
14 Co-tenancy in the Castle Rock Junction-Lakeville 230-kV Transmission Line (“Castle Rock
15 Agreement” or “Agreement”) to PG&E and the other, remaining Cotenants (collectively,
16 “Remaining Cotenants”)² prior to the Petition Date?

17 Did the Castle Rock Agreement terminate as to DWR effective August 1, 2019, pursuant to
18 DWR’s termination notice?

19 Did the terms of the Castle Rock Agreement require that DWR pay for any future, estimated
20 costs of removing the transmission line before its termination could be effective?

21 Did the Castle Rock Agreement constitute an executory contract that could be assumed as
22 to DWR under the Plan at the time of plan confirmation?

23 Is DWR’s Proof of Claim No. 78104 seeking a refund for overpayment of operation and
24 maintenance fees in the principal amount of \$101,026.75 allowed and payable by the Debtors?

25 Do the arbitration provisions in the Castle Rock Agreement preclude the Court from
26 determining whether DWR’s Proof of Claim should be paid?

27 DWR submits that, consistent with the requirements of the Castle Rock Agreement, it gave
28 PG&E and the Remaining Cotenants one-year advance notice that it was terminating its
participation in the Agreement by letter dated July 30, 2018, prior to the Petition Date but effective

² The Remaining Cotenants are Northern California Power Agency (“NCPA”) and the City of Santa Clara, doing business as Silicon Valley Power (“SVP”).

1 August 1, 2019. Pursuant to the Castle Rock Agreement, DWR paid PG&E for operations and
2 maintenance fees in advance for the year of July 1, 2019, through July 31, 2020. However, pursuant
3 to DWR's termination rights exercised in its notice, its participation in the Castle Rock Agreement
4 terminated effective August 1, 2019. Therefore, PG&E is required to refund DWR eleven months
5 of overpayment for operations and maintenance, plus post-petition interest. No amounts are due
6 from DWR for any future, estimated costs of removing the transmission line. The arbitration
7 provisions contained in the Castle Rock Agreement do not preclude the Court from compelling
8 payment of DWR's proof of claim.

9 **III. BACKGROUND**

10 DWR is an agency of the State of California, headquartered in Sacramento. It is responsible
11 for monitoring, conserving, and developing California's water resources, providing public safety,
12 and preventing property damage related to water resources. A primary responsibility of DWR is
13 the construction, operation, and maintenance of the California State Water Project ("SWP"). The
14 SWP is the largest state-owned, multipurpose water project and power generator in the United
15 States. The SWP consists of an integrated network of aqueducts, pumping facilities, reservoirs, and
16 hydroelectric facilities that deliver an average of 2.7 million acre-feet of water per year to 29 public-
17 agency water contractors throughout California. Approximately 40% of the deliveries are used to
18 irrigate approximately 750,000 acres of farmland and the remainder serves the water needs of
19 almost 27 million Californians. Not only does the SWP help California manage its water supply
20 during extremes, such as flooding and drought, but it is also a major source of hydroelectric power
21 deliveries for the State's power grid. (AlQaser Decl. ¶2.)

22 **A. DWR Terminated Its Participation in the Castle Rock Agreement,** 23 **Effective August 1, 2019.**

24 The Castle Rock Agreement is a co-tenancy agreement that became effective as to PG&E,
25 DWR, and the Remaining Cotenants on June 1, 1984 for the purpose of constructing and co-owning
26 a new 230-kV double circuit transmission line between Castle Rock Junction and the PG&E
27 Lakeville Substation ("the Line"). (AlQaser Decl. ¶4, Ex. 1.) Each cotenant owns an undivided
28 interest in the Line. The terms of the Agreement required DWR and the other Cotenants to share

1 the initial costs of construction of the Line and associated facilities and pay annual charges for the
2 associated facilities and the operation and maintenance of the Line in proportion to their ownership
3 interests. (*Id.*, ¶5, Ex. 1, Sections 5.0, 6.0, pp. 33-45.) The initial term of the Castle Rock Agreement
4 extended through December 31, 2014, and continued thereafter from year to year unless terminated.
5 (*Id.*, Ex. 1, Section 14.0, p. 95.)

6 Section 14.3 of the Agreement clearly and unambiguously provides that a Cotenant may
7 terminate participation in the Agreement and provides no conditions on when termination becomes
8 effective other than the one-year advance notice.

9 **Termination By A Cotenant.** Any Cotenant may, by giving one (1) year advance
10 written notice to the other Cotenants, terminate its participation in this Agreement
11 effective no earlier than January 1, 2015.

12 (AlQaser Decl. ¶6, Ex. 1, Section 14.3, p. 97.) Pursuant to Section 14.3, by letter dated July 30,
13 2018, and prior to PG&E filing for bankruptcy, DWR gave one-year advance written notice to
14 PG&E and the Remaining Cotenants that it was terminating its participation in the Castle Rock
15 Agreement, effective August 1, 2019. (*Id.*, Ex 2.) There is no language in the Agreement that gives
16 PG&E or any of the Remaining Cotenants any discretion to reject or deny the termination or its
17 effective date.

18 DWR filed a proof of claim (78104) seeking a refund for overpayment of operation and
19 maintenance fees in the principal amount of \$101,026.75, representing its prepayment for operating
20 and maintenance expenses for 11 months. (AlQaser Decl., ¶15, Ex. 6.)

21 Once DWR gave its termination notice, PG&E and the Remaining Cotenants were required
22 under Section 14.4 of the Agreement to decide whether one or more of them wished to keep
23 operating the Line and buy DWR's interest in the Line. (AlQaser Decl. ¶7, Ex. 1, Section 14.4, p.
24 97.) If there is a unanimous decision to not continue operating the Line, Section 14.5 of the
25 Agreement would apply. This section provides:

26 **14.5 Termination By All Cotenants.** If the remaining Cotenants determine not to
27 continue operating the New Line, this Agreement shall terminate on the date
28 specified in the notice. [PG&E], or its successor as operator of the New Line, shall
remove the New Line, credit the net salvage value of the material, and distribute any

1 net proceeds among the Cotenants in proportion to their Ownership Interests. If the
2 removal is performed at a net loss, [PG&E], or its successor as operator of the New
3 Line, shall be reimbursed by the other Cotenants for their respective shares of such
4 net loss in proportion to their Ownership Interests. Each Cotenant shall be liable for
5 financial obligations incurred by it prior to any termination of this Agreement.

6 (*Id.*, pp. 97-98.)

7 As noted in Section 14.5, had PG&E and the Remaining Cotenants decided not to continue
8 operating the Line, the Agreement would terminate in its entirety on the date specified in the notice,
9 and PG&E or its successor as operator of the Line, would be required to remove the Line, credit
10 the net salvage value of the material and distribute any net proceeds among the Cotenants in
11 proportion to their Ownership Interests. (AlQaser Decl., ¶13.)³ If the removal was performed at a
12 net loss, PG&E, or its successor as operator of the Line, would be reimbursed by the Cotenants for
13 their respective shares of such net loss in proportion to their ownership interests. (*Id.*)

14 Here, PG&E and the Remaining Cotenants decided to continue operating the Line, so
15 Section 14.5 does not apply. (AlQaser Decl. ¶13.) In this situation, because the Cotenants continue
16 to operate the Line, Section 14.6 of the Agreement governs. (*Id.*) Section 14.6 provides:

17 14.6 Continued Operation By Cotenants. If one or more Cotenants wish to continue
18 operating the New Line, the Cotenants wishing to purchase the interest(s) of the
19 departing Cotenant(s) may do so effective as of the date the selling Cotenant
20 terminates its participation in this Agreement. If more than one Cotenant wish to
21 purchase such interest(s), they may do so in proportion to their respective Ownership
22 Interests or as otherwise agreed. All interests available for purchase must be
23 acquired by the purchaser(s). The sale price will be the estimated net salvage value
24 of the interests purchased. The purchasing Cotenant(s) shall pay the departing
25 Cotenant(s) their share of the sale price. The departing Cotenant(s) shall transfer its
(their) interest(s) to the purchasing Cotenant(s) and shall have no more interest in or
liability under this Agreement except with respect to financial obligations incurred
prior to its effective date of termination. The departing Cotenant(s) shall obtain and
provide a full release of any encumbrance of its (their) Ownership Interest prior to
such transfer. The departing Cotenant shall be liable for all financial obligations
incurred by it prior to its effective date of termination. The Ownership Interests of
the remaining Cotenant(s) shall be recalculated as appropriate, under Section 2.2....

26 ³ PG&E interprets “net salvage value” as the after-tax value of the assets after subtracting
27 removal costs, after they are taken out of service, disassembled and sold. Given the age and
28 condition of the facilities, PG&E calculates that the removal costs would actually exceed the resale
value of the facilities. Therefore, PG&E estimates that there is no salvage value associated with the
Line. (AlQaser Decl. ¶13.)

1 (AlQaser Decl. ¶13, Ex. 1, p. 98.)

2 Section 2.2.2.5 of the Agreement states:

3 If a Cotenant elects to terminate its participation in this Agreement pursuant to
4 Article 11.0 and/or 14.0, the Ownership Interests in megawatts and in percent of the
5 non-terminating Cotenants shall increase for those which elect to receive the
6 Ownership Interest transferred by the terminating Cotenant. The Cotenants which
receive no transferred Ownership Interest from the terminating Cotenant shall have
no change in their Ownership Interests.

7 (AlQaser Decl. ¶13, Ex. 1, p. 15.) Because none of the Remaining Cotenants elected to
8 receive DWR's interest, DWR's share effectively reverts back to PG&E.⁴ Section 2.2.1.1
9 of the Agreement states:

10 For [PG&E], the Ownership Interest in megawatts is equivalent to the capacity
11 rating of the New Line minus the sum of the Ownership Interests in megawatts of
12 the Cotenants other than [PG&E].

13 (AlQaser Decl. ¶13, Ex. 1, p. 11.) Section 2.2.2 further states that:

14 Ownership Interests shall be adjusted as provided in this Section 2.2.2. For purposes
15 of payment Under Article 5.0, adjustments of Ownership Interests shall be deemed
16 to take effect on the first day of the calendar month in which the transaction or
change specified in this Section 2.2.2 takes place.

17 (*Id.*, p. 12.) Based on Sections 2.2.1.1 and 2.2.2, as of DWR's effective termination date of August
18 1, 2019, DWR's Interest reverted back to PG&E because PG&E's interest is no longer calculated
19 by subtracting DWR's interest. (AlQaser Decl. ¶13.) Therefore, PG&E's interest increased
20 accordingly.

21 There is a foundational issue arising out of PG&E and the Remaining Cotenants' refusal to
22 accept DWR's termination from the Agreement. They also contend that DWR owes them over \$5
23 million in estimated costs to remove the Line, even though they continue to operate the Line, there
24 are no plans to remove the Line, and removal of the line is not a viable option due to its integration
25 into the California grid for reliability and operational use. (AlQaser Decl., ¶14.) There is no

26 ⁴ See also Section 2.2.2.1 which provides that a Cotenant may terminate its participation in
27 the Agreement within 60 days of executing the Agreement if it was unsatisfied with the quality of
28 PG&E's title to the Land Rights. In this case, the Ownership Interest of the terminating Cotenant
shall revert back to PG&E, and PG&E's interest in megawatts and percentage shall increase
accordingly. (AlQaser Decl., Ex.1, p. 12.)

1 authority in the Agreement to demand future removal costs from a departing Cotenant when there
2 has been no decision by the Remaining Cotenants to discontinue operating the Line, much less
3 demand payment of such removal costs from a cotenant before a termination can become effective.
4 Therefore, DWR effectively terminated its participation in the Agreement and is entitled to a refund
5 of its prepayment of operating and maintenance expenses and PG&E should be ordered to pay its
6 claim.

7 **B. FERC Rejected PG&E's Proposal to Add Language to the Castle Rock**
8 **Agreement Providing that DWR's Termination Would Be Effective**
9 **Pending Payment of Future Removal Costs.**

10 On July 30, 2019, one day before DWR's termination was to become effective, PG&E filed
11 proposed revisions to the Castle Rock Agreement with the Federal Energy Regulatory Commission
12 ("FERC), pursuant to section 205(d) of the Federal Power Act (FPA). (AlQaser Decl. ¶8, Ex. 3.)
13 PG&E proposed to add the following paragraph to section 14.3 of the Agreement:

14 By letter dated July 30, 2018, and pursuant to Section 14.3 of the Agreement,
15 [DWR] gave each of the Cotenants one (1) year advance notice of its desire to
16 terminate [DWR]'s participation in the Agreement, with a requested August 1, 2019
17 effective date for such termination. PG&E, NCPA, and Santa Clara acknowledge
18 [DWR]'s request to terminate its participation in the Agreement, but have rejected
19 [DWR]'s requested withdrawal from the Agreement pending receipt of [DWR]'s
20 payment of its proportional share of the reasonable estimated removal costs to the
21 remaining Cotenants prior to withdrawing from the Agreement. Upon receipt of
22 [DWR]'s payment, PG&E, NCPA and Santa Clara, as the remaining Cotenants,
23 agree to terminate [DWR]'s participation and to file an amended agreement among
24 the remaining Cotenants pursuant to Section 14.2 of the Agreement.

25 The removal costs referenced in the proposed amendment refer to the same costs incurred
26 with removing the Line referenced in Section 14.5 above. (AlQaser Decl. ¶9.) The removal costs
27 are estimated and have not materialized because PG&E and the Remaining Cotenants have decided
28 to not remove the Line and may never do so. (*Id.*) In addition, only DWR would have been required
to pay removal costs under PG&E's proposed amendment to the Castle Rock Agreement. PG&E
also requested waiver of the Commission's prior notice requirements, claiming DWR would not be
harmd, to allow the proposed revisions to the Castle Rock Agreement to become effective July
31, 2019, a day before DWR's termination was to become effective. (*Id.*)

At FERC, PG&E acknowledged DWR's request to terminate its participation in the

1 Agreement, but “rejected” DWR’s request pending receipt of DWR’s payment of its proportional
2 share of the estimated future costs for removing the Line. (AlQaser Decl. ¶8.) DWR intervened and
3 filed a protest, arguing that PG&E improperly added a new term, in the form of a “termination
4 payment,” to the Castle Rock Agreement after DWR already satisfied the termination requirements
5 under Section 14.3. (*Id.*, ¶10, Ex. 4, p. 2.)

6 FERC held that PG&E did not meet its burden to establish that its amendment to the Castle
7 Rock Agreement was just and reasonable. (AlQaser Decl. ¶14, Ex. 5.) FERC found that PG&E’s
8 proposed amendment “is either an improper imposition of a new obligation on DWR without its
9 consent, or an attempt to expressly codify a disputed obligation in the Agreement, notwithstanding
10 that the Agreement already ensures that a departing party remains responsible for all financial
11 obligations incurred while it was a party to the Agreement.” (AlQaser Decl. ¶11, Ex. 5, ¶12, p. 4.)
12 Although FERC reached no conclusion as to the merits of the dispute, it held that PG&E did not
13 adequately justify its proposed changes. (*Id.*)

14 **C. PG&E Objects to Paying DWR’s Claim and Continues to Bill DWR for**
15 **Annual Charges.**

16 PG&E filed for bankruptcy protection on January 29, 2019. DWR filed its proof of claim
17 in the bankruptcy proceeding on October 18, 2019, seeking a refund for the advance payment of
18 the annual facilities charge and operating and maintenance fees it paid PG&E for the period July 1,
19 2019, through July 30, 2020, based on its August 1, 2019, effective termination date from the Castle
20 Rock Agreement. (AlQaser Decl., Ex. 6.) PG&E objects to the claim, although PG&E has yet to
21 file any formal objections to the claim with the Court.

22 As noted above, PG&E incorrectly contends that DWR’s termination is not effective until
23 it pays its share of any future removal costs. However, there is no reference to any obligation to
24 pay for any future removal costs in the Castle Rock Agreement prior to, or as a condition of,
25 effectuating termination. DWR disputes that it has any obligation to pay for future removal costs
26 because PG&E and the Remaining Cotenants did not decide to discontinue operating the Line and
27 remove it in connection with DWR’s termination notice. Pursuant to the terms of the Castle Rock
28 Agreement, DWR effectively terminated its participation in the Agreement as of August 1, 2019.

1 Therefore, DWR has no role, obligation or responsibility in any future decisions made by PG&E
2 and the Remaining Cotenants, including removing the Line. (AlQaser Decl. ¶14.) Yet, PG&E
3 continues to insist that DWR must pay a proportional share of any future removal costs before its
4 termination from the Agreement may become effective, even though PG&E and the Remaining
5 Cotenants continue to operate the Line and removing the Line is not a viable option due to its
6 integration into the California grid for reliability and operational use. (*Id.*) Based on PG&E's
7 erroneous position, PG&E continues to bill DWR for ongoing operating and maintenance expenses
8 and interest that it is no longer obligated to pay because it is no longer a party to the Agreement.
9 (*Id.*)

10 The Court granted PG&E an extension of time until March 23, 2022, to object to DWR's
11 Claim No. 78104. (Dkt. 11533). Pursuant to this Court's Order Approving ADR procedures (Dkt.
12 9148), DWR participated in a mediation with PG&E and the Remaining Cotenants, but the parties
13 were unable to reach a resolution. (AlQaser Decl. ¶16.) The next step should be to resolve DWR's
14 claim in the bankruptcy court pursuant to the retained jurisdiction provisions in the Plan and
15 Confirmation Order for resolving disputes over the assumption of executory contracts and claims
16 objections. The dispute constitutes both a Contract Assumption or Rejection Dispute and Cure
17 Dispute that remains unresolved, as provided in paragraph 32(c) of the Confirmation Order, for
18 which this Court is the proper forum to decide the dispute.

19 **D. Over Three Years After DWR's Notice of Termination, and After Utilizing**
20 **the Court's Authorized ADR Procedures, PG&E Seeks to Enforce**
21 **Arbitration Under the Agreement.**

22 Rather than file any formal objections to DWR's proof of claim, PG&E and the Remaining
23 Cotenants are now seeking to utilize terms in the Castle Rock Agreement that allow for an internal
24 committee process and/or arbitration to resolve the underlying dispute between the parties.
25 (AlQaser Decl. ¶17.) However, the language in the Castle Rock Agreement reveals that these
26 provisions were intended to resolve disputes among the Cotenants while still parties to the
27 Agreement and should not apply to resolve disputes three years after DWR has terminated its
28 participation in the Agreement. Thus, this Court is the forum for resolution of DWR's Claim No.

1 78104 because it relates to the Court's jurisdiction to resolve Contract Assumption or Rejection
2 Disputes and Cure Disputes.

3 IV. ARGUMENT

4 It is basic bankruptcy law that a contract that was terminated pre-petition cannot be assumed
5 in a bankruptcy case. *See In re Sigel & Co.*, 923 F.2d 142, 145 (9th Cir. 1991) (citing *Moody v.*
6 *Amoco Oil Co.*, 734 F.2d 1200, 1212 (7th Cir. 1984) ("If a contract has been terminated pre-
7 bankruptcy, there is nothing left for the debtor to assume."). The Debtors acknowledge this
8 principle in their Plan in Section 8.1(a) as follows:

9 (a) As of, and subject to, the occurrence of the Effective Date and the payment
10 of any applicable Cure Amount, all executory contracts and unexpired leases of
11 the Reorganized Debtors shall be deemed assumed, unless such executory
12 contract or unexpired lease (i) was previously assumed or rejected by the
13 Debtors, pursuant to a Final Order, (ii) **previously expired or terminated**
14 **pursuant to its own terms** or by agreement of the parties thereto, (iii) is the
subject of a motion to assume, assume and assign, or reject filed by the Debtors
on or before the Confirmation Date, or (iv) is specifically designated as an
executory contract or unexpired lease to be rejected on the Schedule of Rejected
Contracts.

15 Plan at § 8.1(a) (emphasis added); *see also*, Confirmation Order ¶ 32(a)(ii) (same language).

16 In connection with confirmation of the Plan, the Debtors filed a Notice of Filing of Plan
17 Supplement in support of the Plan (Dkt. 7037), which contained as Exhibit B the list of executory
18 contracts the Debtors expected would be assumed under the Plan. The California State Agencies,
19 including DWR, filed their objections to the list of contracts to be assumed and the proposed cure
20 amounts. (Dkt. 7276.) In that objection, *inter alia*, the California State Agencies noted their
21 objection that the descriptions of the purported contracts on Exhibit B were not sufficient for a
22 contract counterparty to ascertain the document being referenced to be able to determine whether
23 the item is an executory contract. Due to that lack of specificity, to this day it is unclear whether
24 the Castle Rock Agreement is listed in Exhibit B as a purported contract to be assumed.⁵ Further,
25 the Confirmation Order at paragraph 67(d) preserves any rights of a Governmental Unit to object

26
27 ⁵ As noted above, the Plan at section 8.1(a) provides that all executory contracts to be
28 deemed assumed unless they are rejected or were terminated. DWR is informed and believes that
the Castle Rock Agreement was not rejected. Thus, whether the Castle Rock Agreement was listed
or not is not pertinent to the analysis.

1 to the assumption of any executory contract (which the California State Agencies had already done
2 by Dkt. 7276). Regardless, the California State Agencies, including DWR, preserved their rights to
3 object to the assumption of any executory contract with a state agency.

4 The Plan and the Confirmation Order provide that in the event of an unresolved dispute over
5 “any matter pertaining to the assumption,” such dispute shall be resolved by Final Order of the
6 Court, which may be entered after the Effective Date. *See* Plan §8.2(c) and Confirmation Order ¶¶
7 34(a) and (b) and 67(d) (“any such dispute shall be resolved by the Bankruptcy Court.”). Further,
8 the Plan and Confirmation Order specifically reserve the Court’s jurisdiction over all matters arising
9 from or related to the implementation of the Confirmation Order and to hear any disputes involving
10 the assumption of executory contracts and the allowance of any Claims resulting therefrom. *See*
11 Plan §11.1(a); Confirmation Order ¶ 78.

12 There is now a dispute between DWR and PG&E as to whether the Castle Rock Agreement
13 was terminated and thus could not be assumed, and over the payment of DWR Claim No. 78104.
14 It is DWR’s position that the Castle Rock Agreement was terminated as to DWR prior to the Petition
15 Date (but effective August 1, 2019), and that the arbitration provisions in the Agreement do not
16 apply to the resolution of Claim No. 78104 or any related claims PG&E may raise in defense about
17 the claim. DWR contends that this Court should determine the issues presented herein under its
18 retained jurisdiction and other provisions of the Plan and Confirmation Order covering disputes
19 over executory contract issues. This dispute is a Contract Assumption or Rejection Dispute that
20 remains unresolved.

21 The Court should find that DWR terminated its participation in the Castle Rock Agreement
22 such that the Agreement could not be assumed as to DWR and that PG&E must pay the
23 overpayment claim in the principal amount of \$101,026.75 plus post-petition interest under the
24 Plan.

25 **A. DWR Properly Terminated Its Participation in the Castle Rock**
26 **Agreement.**

27 Section 14.3 of the Castle Rock Agreement expressly provides that any Cotenant may
28 terminate its participation in the Agreement by giving one year advance written notice to PG&E

1 and the other Cotenants. The language of Section 14.3 is clear and unambiguous. No other action
2 is necessary.

3 The court's "function is to determine what, in terms and substance, is contained in the
4 contract, not to insert what has been omitted. [Courts] do not have the power to create for the parties
5 a contract that they did not make and cannot insert language that one party now wishes were there."
6 *Dameron Hosp. Assn.*, 229 Cal. App. 4th at 569 (quoting *Vons Companies, Inc. v. United States*
7 *Fire Ins. Co.*, 78 Cal. App. 4th 52, 58-59, 92 Cal. Rptr. 2d 597 (2000)); *Integral Dev. Corp. v.*
8 *Tolat*, No. 12-CV-06575-JSW (JSC), 2016 U.S. Dist. LEXIS 187832, 2016 WL 8929073, at *6
9 (N.D. Cal. Dec. 23, 2016) (court's role limited to "interpret[ing] the terms of the contract, [] not to
10 add, subtract, or vary the words of the written agreement."). ⁶

11 DWR complied with the provisions of Section 14.3 and gave PG&E and the Remaining
12 Cotenants one-year advance written notice on July 30, 2018 (prior to the Petition Date) that it was
13 terminating its participation in the Castle Rock Agreement, effective August 1, 2019. Therefore,
14 DWR properly terminated its participation in the Castle Rock Agreement prior to June 2020 when
15 the Debtors' Plan was confirmed and executory contracts were assumed in connection with plan
16 confirmation.

17 **B. The Effective Date of DWR's Termination From the Castle Rock**
18 **Agreement Was Not Contingent on Payment of Future Removal Costs.**

19 By demanding that DWR pay speculative or any future removal costs before its termination
20 can become effective, PG&E and the Remaining Cotenants conflate the termination provisions in
21 Section 14.3 with other provisions in the Castle Rock Agreement, producing a new obligation for
22 DWR. Once DWR gave notice of termination, the Remaining Cotenants were required under the
23 terms of the Castle Rock Agreement to decide whether to: (1) continue operating the Line and
24 purchase DWR's ownership interest pursuant to Section 14.4, or (2) discontinue operating the Line
25 and terminate the Castle Rock Agreement pursuant to Section 14.5. Only if PG&E and the
26 Remaining Cotenants decided to terminate the Castle Rock Agreement (which they did not) does

27 ⁶ Section 16.5 of the Castle Agreement provides that it shall be interpreted, governed by,
28 and construed under the laws of the state of California or the laws of the United States, as
applicable...."

1 the sharing of removal costs become an obligation for DWR.

2 Despite the clarity in the Agreement as to when a Cotenant may be responsible for paying
3 any removal costs, PG&E and the Remaining Cotenants erroneously interpret the language in
4 Section 14.6, which states that a departing Cotenant shall be responsible for “financial obligations”
5 incurred prior to its effective date of termination, to require DWR to make a financial contribution
6 to PG&E and the Remaining Cotenants that reflects a proportional share of the reasonably
7 anticipated removal costs of the Line. (See AlQaser Decl., Ex. 5, ¶11.) However, Section 14.6 does
8 not refer to payment of any future removal costs. Removal costs were negotiated and included in
9 the contract under Section 14.5 only for the situation where all the cotenants decided to terminate
10 the Agreement. Section 14.6 applies when the Remaining Cotenants wish to continue operating
11 the Line - exactly the scenario present here. In addition, because any removal of the Line is to occur
12 sometime in the future when the Remaining Cotenants and any future cotenants decide, if ever, to
13 terminate the Agreement, costs associated with that future removal cannot be a “financial
14 obligation” that was “incurred” prior to the time that DWR’s termination became effective within
15 the meaning of Section 14.6.

16 Moreover, at the time of drafting, the parties to the Castle Rock Agreement were well aware
17 of the meaning of future removal costs and knew how to, and did, express when such costs, and
18 other expenses, would be owed from a Cotenant. Had the parties intended for a departing Cotenant
19 to pay future removal costs prior to terminating its interest in the Castle Rock Agreement while the
20 Line was still operating, they would have expressed it in the Agreement. PG&E and the Remaining
21 Cotenants cannot escape the fact that there is no language in the Castle Rock Agreement that
22 requires any Cotenant to make a financial contribution that reflects its proportional share of future
23 removal costs before its participation in the Agreement can be terminated, and such a requirement
24 should not be read into the Castle Rock Agreement. To do so would be contrary to the language in
25 the Agreement and give PG&E and the Remaining Cotenants a windfall, at the expense of DWR.

26 **C. PG&E Owes DWR \$101,026.75 Plus Post-Petition Interest for**
27 **Overpayments of Operation and Maintenance Charges.**

28 Based on DWR’s effective termination date of August 1, 2019, PG&E owes DWR a refund

1 for advance payment of the annual charges and operating and maintenance fees over a period of 11
2 months (August 1, 2019 through July 30, 2020.) (AlQaser Decl. ¶15.) Post-petition interest is also
3 proper based on the Plan’s treatment of Utility General Unsecured Claims at section 4.23(a). Plan
4 §4.23(a) (“The Allowed amount of any Utility General Unsecured Claim shall reflect all interest
5 accrued from the Petition Date through the date of distribution at the Federal Judgment Rate.”).

6 **D. The Arbitration Provisions in the Castle Rock Agreement Do Not Preclude**
7 **Payment of DWR’s Claim.**

8 “Arbitration is strictly a matter of consent and ‘thus is a way to resolve those disputes – but
9 only those disputes – that the parties have agreed to submit to arbitration.’” *Granite Rock Co. v.*
10 *Int’l Bhd. of Teamsters*, 561 U.S. 287, 299 (2010) (citing *Volt Information Sciences, Inc. v. Board*
11 *of Trustees of Leland Stanford Junior Univ.*, 489 U.S. 468, 479 (1989) and *First Options of*
12 *Chicago, Inc. v. Kaplan*, 514 U.S. 938, 943 (1995). “A court may order arbitration of a particular
13 dispute only where the court is satisfied that the parties agreed to arbitrate that dispute.” *Id.* at 297.
14 See also *Goldman Sachs & Co. v. City of Reno*, 747 F.3d 733, 742 (9th Cir. 2014).

15 When determining whether parties have agreed to submit to arbitration, the court applies
16 general state-law principles of contract interpretation. *Mundi v. Union Sec. Life Ins. Co.*, 555 F.3d
17 1042, 1044 (9th Cir. 2009). Arbitration is based on a contractual agreement and therefore the court
18 must look to the wording and scope of the arbitration clause in the parties’ contract to determine its
19 application. *Parker v. Twentieth Century-Fox Film Corp.*, 118 Cal. App. 3d 895, 901 (Cal. Ct. App.
20 2 Dist. 1981) (citing *Freeman v. State Farm Mut. Auto Ins. Co.*, 14 Cal. 3d 473, 479 (1975)). The
21 Court “should attempt to give effect to the parties’ intentions, in light of the usual and ordinary
22 meaning of the contractual language and the circumstances under which the agreement was made.”
23 *Victoria v. Superior Court*, 40 Cal. 3d 734, 744 (1985).

24 To determine whether a contractual arbitration clause covers a particular dispute, the court
25 engages in a two-step inquiry. First, the court determines whether the arbitration clause is broad or
26 narrow in scope and then applies the breadth of the provision to the legal claims asserted to
27 determine whether they must be arbitrated. See *Simula, Inc. v. Autoliv, Inc.*, 175 F.3d 716, 720-26
28 (9th Cir. 1999). “A ‘broad’ clause includes those using language such as ‘any claim arising from or

1 related to this agreement’ or ‘arising in connection with this agreement.’” *Rice v. Downs*, 248 Cal.
2 App. 4th 175, 186 (Cal. Ct. App. 2 Dist. 2016) (citing *Simula* at 720). A broad clause reaches every
3 dispute between the parties and may extend to tort claims that may arise under or from the
4 contractual relationship. *Simula* at 721. By contrast, a “narrow” clause is one that only employs
5 language such as “arising from” or “arising out of” an agreement, excluding more broader language
6 such as “relating to” or “in connection with.” *Rice* at 186.

7 Section 13.2 of the Castle Rock Agreement states: “Disputes arising under this Agreement
8 *that have not been resolved under Sections 13.1 [Submittal of Dispute to Coordinating Committee]*
9 *or 15.2.3 [review by Coordinating Committee]* shall be settled through binding arbitration as
10 provided in this Section 13.2 (emphasis added).” This language suggests that Section 13.2 is a
11 narrow clause because it qualifies the disputes that can be settled via arbitration (i.e., those that
12 have not been resolved by the Coordinating Committee), and that arbitration is intended to resolve
13 disputes that arise while a cotenant is still a party to the Agreement. For example, Section 13.1
14 provides that any billing dispute or any other dispute arising under the Castle Rock Agreement must
15 be submitted to a Coordinating Committee by a Cotenant involved in the dispute. The Committee
16 will attempt to settle all disputes no later than 45 days after the dispute is submitted, unless an
17 extension is agreed upon by the Cotenants involved in the dispute. (*Id.*) No Cotenant shall
18 commence arbitration of any dispute until after the 45-day period. (*Id.*)

19 Section 15 of the Castle Rock Agreement defines the structure, function and responsibilities
20 of the Coordinating Committee. The Committee is comprised of a Chairperson, who is a
21 representative of PG&E, and no more than two representatives appointed by each Cotenant (Section
22 15.1.) The Committee serves as liaison between PG&E and the other Cotenants, and to provide a
23 forum for discussion of a number of performance, operational and maintenance issues. (Sections
24 15.2.1-15.2.3.4; 15.2.4 [requests for maintenance, capital replacements, additions, betterments and
25 changes in points of connection].)

26 The language in Sections 13 and 15 of the Castle Rock Agreement show that the primary
27 purpose of the dispute resolution procedures is to resolve issues relating to billing and performance
28 and operational issues that arise while the Cotenants are still participating in the Agreement. Such

1 provisions should not be interpreted to apply to a party that is no longer a Cotenant to the
2 Agreement.

3 In addition, resolution of DWR's proof of claim and the Contract Assumption or Rejection
4 Dispute are core issues that the Court should resolve. 28 U.S.C. § 157(b)(2)(A), (B), (C), and (O);
5 *see also, Republic Underwriters Ins. Co. v. DBSI Republic, LLC (In re DBSI, Inc.)*, 409 B.R. 720,
6 728 (Bankr.D.Del.2009) (challenges as to the effect of orders under § 365 are core, as "the rejection
7 and assumption and assignment of leases and executory contracts are fundamental issues of
8 bankruptcy law unique to the Bankruptcy Code."); *see also Agent Sys., Inc. v. Capital Metro.*
9 *Transp. Auth. (In re Agent Sys., Inc.)*, 289 B.R. 828, 833 (Bankr.N.D.Tex.2002) ("by filing a motion
10 to assume the Contract, Debtor triggered this court's core jurisdiction over other proceedings
11 dealing with the same subject matter"); *Liona Corp., N.V. v. PCH Assoc. (In re PCH Assoc.)*, 60
12 B.R. 870, 872–73 (S.D.N.Y.1986) (adversary proceeding to recharacterize a lease was a core claim
13 because that issue was central to a related § 365 motion); *see also, Point Blank Solutions, Inc. v.*
14 *Robbins Geller Rudman & Dowd LLP (In re Point Blank Solutions, Inc.)*, 449 B.R. 446, 450 (Bankr.
15 D. Del. 2011) (claims that arise directly from the substantive bankruptcy law right to reject
16 executory contracts are a fundamental issue of bankruptcy law unique to the Bankruptcy Code.).

17 "In core proceedings . . . the bankruptcy court, at least when it sees a conflict with
18 bankruptcy law, has discretion to deny enforcement of an arbitration agreement." *In re Thorpe*
19 *Insulation Co.*, 671 F.3d 1011, 1021 (9th Cir. 2012). "[T]he core/non-core distinction, though
20 relevant, is not alone dispositive." (*Id.*) That is, "even in a core proceeding ... a bankruptcy court
21 has discretion to decline to enforce an otherwise applicable arbitration provision only if arbitration
22 would conflict with the underlying purposes of the Bankruptcy Code." (*Id.*) "[T]he purposes of the
23 Bankruptcy Code include 'centralization of disputes concerning a debtor's legal obligations' and
24 'protect[ing] creditors and reorganizing debtors from piecemeal litigation.'" (*Id.* at 1022.)

25 DWR has filed a proof of claim in the bankruptcy case. Allowing or disallowing DWR's
26 claim raises executory contract and cure dispute issues that are unique to, and should be decided
27 by, the bankruptcy court. The Ninth Circuit's decision in *In re Thorpe Insulation Co.* is on point:
28

1 Here, we agree with the bankruptcy court and the district court that the resolution of
2 Continental's claim was a core proceeding. Continental argues that its "state law
3 breach of contract claim" is non-core because "it is based on state law and arose
4 outside of and independent of Thorpe's bankruptcy." Yet regardless of how
5 Continental characterizes its claim, Continental filed a proof of claim, and Thorpe
6 objected to the claim, so under 28 U.S.C. § 157(b)(2)(B), the allowance or
7 disallowance of that claim was a core proceeding. *In re Thorpe Insulation Co.* at
8 1021 (citing *Durkin v. Benedor Corp.* (In re G.I. Indus. Inc.), 204 F.3d 1276, 1279-
9 80 (9th Cir. 2000) ("The filing of a proof of claim is the prototypical situation
10 involving the 'allowance or disallowance of claims against the estate,' a core
11 proceeding under 28 U.S.C. § 157(b)(2))." See also *J.W. McClenahan Co. v. Mech.*
12 *Techs. Corp.*, 2020 U.S. Dist. LEXIS 71064 at 3-4 (N.D. Cal. Apr. 21, 2020)
13 ("Given that the filing of the proof of claim in the bankruptcy subjects the claim to
14 the bankruptcy court's jurisdiction, the Court agrees that the filing extends to the
15 interrelated actions . . .").

16 Under *In re Thorpe Insulation Co.*, the allowance or disallowance of DWR's claim, as a
17 proof of claim filed against the estate, is similarly a core proceeding. See also *In re Conejo Enters.,*
18 *Inc.*, 96 F.3d 346, 354 (9th Cir. 1996) ("Once [a party] filed its proof of claim, it subjected its claim
19 to the core jurisdiction of the bankruptcy court."). As such, the Court has discretion to retain
20 jurisdiction over DWR's claim and not send adjudication of the claim to arbitration.

21 The Court should exercise its discretion and retain jurisdiction to resolve DWR's proof of
22 claim, PG&E's defenses to payment of such claim, and this Contract Assumption or Rejection
23 Dispute. Doing so is not only proper under the specific terms of the Plan and Confirmation Order,
24 but also will promote the underlying purpose of centralization of the Debtors' legal obligations and
25 protect DWR from piecemeal litigation. To the extent that PG&E and the Remaining Cotenants
26 argue that DWR's termination was not effective pending payment of its proportional share of future
27 removal costs, these issues must be resolved by this Court as part of resolving the Contract
28 Assumption or Rejection Dispute and any objections to DWR's claim.

29 This Court may also find that PG&E and the Remaining Cotenants waived arbitration by
30 waiting over three years to seek such relief, and after unsuccessfully seeking a solution at FERC to
31 gain a litigation advantage. "[I]n the absence of legal excuse, a party's failure to timely demand
32 arbitration results in a contractual forfeiture of the right to compel arbitration." *Platt Pacific, Inc.*
33 *v. Andelson*, 6 Cal. 4th 307, 318-19 (1993).

1 In determining waiver, a court can consider (1) whether the party's actions are inconsistent
2 with the right to arbitrate; (2) whether the litigation machinery has been substantially invoked and
3 the parties were well into preparation of a lawsuit before the party notified the opposing party of
4 an intent to arbitrate; (3) whether a party either requested arbitration enforcement close to the trial
5 date or delayed for a long period before seeking a stay; (4) whether a defendant seeking arbitration
6 filed a counterclaim without asking for a stay of the proceedings; (5) whether important intervening
7 steps (e.g., taking advantage of judicial discovery procedures not available in arbitration) had taken
8 place; and (6) whether the delay affected, misled, or prejudiced the opposing party.

9 *Wagner Construction Co.*, 41 Cal. 4th 19, 22-23 (2007).

10 PG&E and the Remaining Cotenants have not displayed a good faith belief that DWR is
11 still a party to the contract and that the arbitration provisions in the Agreement are effective or even
12 applicable, given that they had over three years to seek review through the Coordinating Committee
13 process and/or arbitration, but declined to do so. Since DWR exercised its termination rights under
14 the Agreement, PG&E filed for bankruptcy, delaying DWR's receipt of its refund for prepaid
15 operating and maintenance expenses. PG&E acted inconsistently with its right to use the dispute
16 resolution procedures in the Agreement by waiting until after FERC rejected its unilateral attempt
17 to modify the language in the Agreement to DWR's detriment. Any attempt to invoke the dispute
18 resolution procedures and/or arbitration provisions in the Agreement now is prejudicial to DWR
19 because it is no longer a party to the Agreement and has been waiting for over two years for its
20 proof of claim to be resolved in the bankruptcy court.

21 V. CONCLUSION

22 For the reasons set forth above, DWR seeks an order determining that: (1) DWR's cotenant
23 interest in the Castle Rock Agreement terminated on its own terms, effective August 1, 2019, based
24 on DWR's July 30, 2018, written notice to Pacific Gas & Electric Company ("PG&E") and the
25 other cotenants to the Agreement; (2) the terms of the Castle Rock Agreement do not require that
26 DWR pay for any future estimated costs of removing the transmission line before its termination
27 from the Agreement could become effective; (3) because DWR's termination of its cotenant interest
28 in the Castle Rock Agreement became effective on August 1, 2019, it is not an executory contract

1 that could have been assumed by Co-Debtors PG&E and PG&E Corporation in connection with
2 Plan and Confirmation Order on June 19, 2020; (4) DWR's proof of claim No. 78104 in the
3 principal amount of \$101,026.75 for a refund of prepaid annual operating and maintenance
4 expenses under the Castle Rock Agreement should be paid with post-petition interest under the
5 Plan; (5) the arbitration provisions contained in the Castle Rock Agreement do not preclude the
6 Court from determining whether DWR's proof of claim should be paid; and (6) for such other and
7 further relief as the Court deems just.

8
9 Dated: February 1, 2022

Respectfully submitted,

10 ROB BONTA
11 Attorney General of California
12 DANETTE VALDEZ, SBN 141780
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15 By:

16 /s/ Paul J. Pascuzzi
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20 Attorneys for California Department of
21 Water Resources, by and through the State
22 Water Project

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I am a resident of the State of California and over the age of eighteen years, and not a party to the within action; my business address is 500 Capitol Mall, Suite 2250, Sacramento, CA 95814. On February 1, 2022, I served the within documents:

By Electronic Service only via CM/ECF.


Susan R. Darms